Surviving the Annual Audit

Practical Advice for a Successful and Stress-Free Financial Statement and Performance Measures Audit.

- Introduction
- Practical Tips
  - Pre-Audit Planning
  - Communication with Staff
  - Audit Arrival
- Post Audit Activities
- Reference

Introduction

The fiscal year end is approaching quickly, which means the annual audit is right around the corner. While many find the annual audit to be stressful, it doesn't have to be. Working together with the auditor can yield many benefits including:

- less time spent by your staff providing information and fielding questions
- fewer disruptions to your work process
- feedback to assist you in improving your performance and internal controls
- timely release of audited financial statements

The purpose of this document is to provide some practical tips that will help the audit process run more smoothly and to minimize frustrations.

Intended Audience

This document is intended for controllers, chief financial officers, and others who are involved in the audit at the year end.

Practical Tips

A. Pre-Audit Planning

Pre-audit planning is critical to ensure that the whole process runs smoothly. It involves the following:

1. Setting of Deadlines

   The following dates should be determined and agreed upon with the auditor prior to the year end:

   a. Entrance meeting
   b. Commencement and completion of interim audit fieldwork
   c. Completion of draft financial statements by auditee
   d. Commencement and completion of final audit field work
   e. Exit conference meeting
   f. Audit Committee meeting
   g. Release of audited financial statements

   Setting dates early establishes the critical path for timely financial statement preparation.

2. Compilation of an "Information Needs" List

   An "information needs" list should be compiled by the auditor and provided to you. This list should itemize schedules and working papers required by the auditor for each financial statement component along with the scheduled completion date. Responsibility for the preparation of each schedule should be assigned to specific employees immediately by your office, and this information communicated to the auditor.

   Schedule and working paper formats should be determined and agreed upon by both yourself and the auditor. This should minimize the time spent by your staff in assembling the information, and avoid the need to revise the material.

   The "information needs" list should be provided to you prior to the commencement of the final audit fieldwork. This will allow you to review the information requested and discuss any concerns you may have about the content or completion dates well in advance of the critical audit deadline. If you have not received a copy of such a list, please contact your auditor.

An effective way of providing the auditor with the schedules and documentation identified in the "information needs" list is by assembling a well structured financial statement file. A good file that supports the preparation of financial statements will decrease questions and information requests by the auditor. A good file has the following characteristics:

- It supports all numbers in the financial statements, including numbers on the statement of changes in financial position, as well as all numbers presented in the notes.
- It includes all schedules and reports used to compile the financial statement numbers. The schedules and reports should tie directly to the accounting records. This should be done in such a way that one is easily able to see that all accounts in the trial balance have been completely accumulated in the financial statements.
- The organization of the file should be driven by the financial statement components. For example, the file could be organized in order of assets, liabilities, revenues and expenses.

Explanations of significant variances from year to year will always be required by the auditors. Analytical review is a valuable tool for understanding the nature of changes in the balances and transactions of an organization and in evaluating the reasonableness of the numbers. An analysis of significant changes should be incorporated in the supporting file. A good analytical review will incorporate:

- A description of the nature of the component (ie, what is it comprised of).
- A description of what occurred during the year, and whether that is reasonable given the nature of the component.

3. Functioning Internal Controls

Professional standards require the auditor to obtain a reasonable understanding of internal controls in order to plan the audit. Documenting the systems of internal controls, or updating existing documentation, can be made more efficient by having the appropriate staff from your office assist the auditor in obtaining this information.

If there are any significant changes in specific internal controls, you

should inform the auditor at once so that:

- the potential impact of the changes can be assessed well in advance of the critical audit completion target; and
- audit plans can be adjusted accordingly.

B. Communication with Staff

Dealings between your staff and the auditors can be made more productive when each understands the other's expectations and needs. This can be facilitated by the following:

- Designate an audit coordinator. The audit coordinator should know every aspect of your financial operation and be able to answer or direct to the appropriate individual, the external auditor's questions about internal controls, financial statements, policy and procedures and any systems used by the organization. Both your staff and the audit staff should be made aware of who the audit coordinator is and the types of audit related concerns they can bring to this person. This individual should not be the sole contact however; merely a provider of information and contacts.
- Have your staff mark their calendars when the auditor will be performing the interim and final fieldwork and let them know they should be available to the auditors during this time.
- Distribute the "information needs" list to the appropriate staff responsible for the information preparation. Staff should mark the schedule or working paper completion date on their calendars. As well, it may be useful to meet with staff a few weeks prior to the arrival of the auditors to assess their progress.
- Determine your priorities and communicate these to your staff. There will likely be conflicts that your staff will encounter between the auditor's needs and the normal duties of your staff. Significant conflicts should be resolved by the audit coordinator.

C. Audit Arrival

When the auditors arrive it is important to ensure that they have the necessary resources to complete their audit work as quickly and efficiently as possible. The following suggestions are made to facilitate the audit process:

- Introduce the auditors to the audit coordinator and discuss the types of questions and concerns that can be brought to the coordinator's

attention.

- A contact list should be provided to the auditors. It should note the key people for each section, their phone numbers and office locations.
- Assign an individual to locate documents for the auditors. Your staff should be able to gather information quicker and with less disruption than the auditors could.
- An appropriately sized room or desk space, phone, storage space, secure filing, parking spots etc. should be arranged and ready for the auditor's arrival. Discuss these needs with the audit senior one to three weeks prior to their arrival to ensure that the needed resources will be ready.
- A binder that includes a photocopy of all schedules requested, draft financial statements and other necessary working papers should be prepared and ready for the auditors on their arrival.
- Frequent chats with the audit senior should be arranged to discuss the progress of the audit, problems or difficulties encountered, etc. This will help keep each other informed of both the audit progress and accounting staff concerns in order to minimize last minute difficulties and/or problems.

Post Audit Activities

The annual audit process can always be improved. At the conclusion of the audit, a meeting between the audit senior and the audit coordinator should be held to discuss achievements, problems encountered, and possible solutions for the problems. Each party should give feedback on how the other performed during the audit, so that the lessons learned about what didn't work can be used to improve the process in the following year.

Reference

Journal of Accountancy, January 1998

Back

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Last updated: Friday, May 5, 2006